Knueven, Schroeder & Co.
CERTIFIED PUBLIC ACCOUNTANTS
Jerome B. Schroeder, CPA
Douglas E. Schleucher, CPA
Ann E. Woolum, CPA/ABV, CBA
Timothy J. Gephart, CPA
Mark L. Schroeder, CPA
Richard D. Hillabrand, CPA
Angela L. Bursby, CPA
Jeffrey C. Quinlan, CPA

Balance *sheet*

Sale of Principal Residence

By Thomas Tomlins

When taxpayers sell their principal residence during the year, the gain on the sale of the house has the potential to be taxable to them. However, as long as the taxpayer meets certain requirements, the gain from the sale of the home can be excluded from taxation.

In general terms, $250,000 of gain can be excluded from the sale of your personal residence as long as the following conditions have been met:

1. Ownership and Use Test: You must have owned and used the home as a principal residence for at least two out of five years prior to the sale. These two years do not have to be consecutive years.
2. Frequency Test: You can only use the exclusion for one sale every two years.

Married filing jointly clients can qualify for a $500,000 exclusion as long as the following conditions have been met:

1. Ownership Test: Either or both spouses must have owned the residence for at least two out of five years.
2. Use Test: Both spouses must have used the home as their primary residence for at least two out of five years.
3. Frequency Test: During the two-year period ending on the date of the sale, neither spouse could have excluded the gain on the sale of a different home.

Even if a taxpayer fails the ownership, use, or frequency tests, they can still qualify for a reduced exclusion if the sale of the home was due to:

1. Change in place of employment
2. Health
3. Unforeseen circumstances

A sale or exchange is by reason of unforeseen circumstances if the primary reason for the sale or exchange is the occurrence of an event that the taxpayer does not anticipate before purchasing and occupying the residence. Unforeseen circumstances that are eligible for the reduced exclusion include involuntary conversions; certain disasters or acts of war or terrorist attacks; death; cessation of employment; change of employment resulting in the taxpayer's inability to pay certain costs; divorce or legal separation; multiple births from the same pregnancy; and events identified by IRS as unforeseen circumstances (for example, the September 11 terrorist attacks).

The amount of the reduced exclusion equals a fraction of the $250,000/$500,000 dollar limitation. The fraction is based on the portion of the two-year period in which the seller satisfies the ownership and use requirements. For example, if you have owned and used your home for one year, a single individual's exclusion would be $125,000 ($250,000 for certain joint filers).

If you are planning on selling a home and would like to discuss how these rules apply to your particular situation, please contact us.